



STATE OF MAINE REVENUE FORECASTING COMMITTEE

Members:

Jerome Gerard, Chair, Acting State Tax Assessor
James Breece, University of Maine System
Marc Cyr, Principal Analyst, Office of Fiscal and Program Review
Ryan Low, State Budget Officer
Grant Pennoyer, Director, Office of Fiscal and Program Review
Catherine Reilly, State Economist

December 1, 2006

TO: Governor John Baldacci
Members-elect, 123rd Legislature

FROM: Jerome Gerard, Chair
Revenue Forecasting Committee

RE: **Summary of December 2006 Revenue Forecast**

The Revenue Forecasting Committee (RFC) has concluded its review of the revenue forecast and has revised its revenue projections through the fiscal years ending June 30, 2009 for the General Fund, Highway Fund, Fund for a Healthy Maine and the Medicaid Dedicated Revenue Taxes to comply with the statutory December 1st reporting date. As the Legislature enters a new budget biennium, this forecast extends the forecast period through the fiscal year ending June 30, 2011 (FY11).

The changes to this revenue forecast are primarily driven by continuous gains in non-traditional economic measures such as capital gains, dividend income, and business income. The Revenue Forecasting Committee felt comfortable making these changes to the forecast after taking into consideration the recent modest forecast by the Consensus Economic Forecasting Committee of traditional economic measures such as employment, income growth, and inflation which were not significant factors in the adjustments made by the RFC. This memo and attachments summarize the results of the December revenue forecast. A more detailed report will be available early in December. Provided below are the summaries of the aggregate forecast for these funds.

Summary of Revenue Revisions

General Fund Summary

	FY06 Actual	FY07	FY08	FY09	FY10	FY11
Current Forecast	\$2,931,825,687	\$2,934,190,370	\$2,988,997,412	\$3,064,864,549		
Annual % Growth	5.1%	0.1%	1.9%	2.5%		
Net Increase (Decrease)		\$86,417,340	\$87,483,151	\$93,405,601		
Revised Forecast	\$2,931,825,687	\$3,020,607,710	\$3,076,480,563	\$3,158,270,150	\$3,262,017,710	\$3,318,238,572
Annual % Growth	5.1%	3.0%	1.8%	2.7%	3.3%	1.7%

Highway Fund Summary

	FY06 Actual	FY07	FY08	FY09	FY10	FY11
Current Forecast	\$326,546,157	\$340,392,025	\$346,268,833	\$353,665,022		
Annual % Growth	0.1%	4.2%	1.7%	2.1%		
Net Increase (Decrease)		(\$9,634,696)	(\$5,272,534)	(\$6,468,502)		
Revised Forecast	\$326,546,157	\$330,757,329	\$340,996,299	\$347,196,520	\$350,245,413	\$356,494,765
Annual % Growth	0.1%	1.3%	3.1%	1.8%	0.9%	1.8%

Fund for a Healthy Maine Summary

	FY06 Actual	FY07	FY08	FY09	FY10	FY11
Current Forecast	\$46,476,908	\$43,689,284	\$73,861,352	\$75,844,458		
Annual % Growth	-5.4%	-6.0%	69.1%	73.6%		
Net Increase (Decrease)		\$2,500,060	(\$13,452,402)	(\$13,028,510)		
Revised Forecast	\$46,476,908	\$46,189,344	\$60,408,950	\$62,815,948	\$67,818,647	\$71,548,715
Annual % Growth	-5.4%	-0.6%	30.8%	4.0%	8.0%	5.5%

Medicaid/MaineCare Dedicated Revenue Taxes Summary

	FY06 Actual	FY07	FY08	FY09	FY10	FY11
Current Forecast	\$118,096,040	\$120,142,902	\$121,472,242	\$122,834,815		
Annual % Growth	23.6%	1.7%	1.1%	1.1%		
Net Increase (Decrease)		\$1,383,102	\$1,353,391	\$1,322,937		
Revised Forecast	\$118,096,040	\$121,526,004	\$122,825,633	\$124,157,752	\$125,523,174	\$126,922,732
Annual % Growth	23.6%	2.9%	1.1%	1.1%	1.1%	1.1%

For the **General Fund**, this forecast increases the previous forecast primarily as a result of the recent positive variances in FY06 in the Corporate and Individual Income Tax categories. It was the view of the committee that strong income gains among upper income earners, a continuation of solid corporate profits growth and double-digit stock market gains in 2006 will not only sustain the level of income tax receipts in FY06, but result in modest growth during the upcoming biennium. Positive variances in the current fiscal year led to a substantial revision upward in the Estate Tax in the current year and smaller upward revisions in future years.

Unlike income and estate taxes, the Sales and Use Tax was adjusted down in this forecast. While the recent decline in energy prices has certainly helped household budgets, the on-going correction in the housing market, high consumer debt and a weak market for automobile sales are projected to keep the growth in sales tax receipts well below the growth in household income during the next 12 to 18 months. Insurance Companies Tax was also revised downward.

Other changes worth noting include upward revisions to the Real Estate Transfer Tax, Parimutuel and Gaming Revenue and the State Cost Allocation Program. Notable reductions include revenue from Targeted Case Management at the Department of Health and Human Services and the recently enacted Transfer to the Maine Milk Pool.

A significant portion of the committee's deliberations focused on the latest data from state and federal income tax returns that show the vast majority of recent taxable income gains have gone to households with incomes greater than \$100,000 a year. The source of these gains has been from bonus income, capital gains, dividend, and business income that traditionally go to upper-income taxpayers. In addition, the recent increases in corporate income tax receipts are unprecedented. Any shock to the U.S. economy, either internally or externally, could result in a reversal of these revenues that is disproportionate to the underlying impact on traditional economic measures. It is with this understanding that the committee once again wants to

convey to the Administration and the Legislature that there is a high level of risk that surrounds this forecast.

For the **Highway Fund**, this forecast decreases FY07 budgeted revenue by \$9.6 million and decreases the previous projections for the 2008-2009 biennium by \$11.7 million. The downward revisions to Fuel Taxes are the major driver of the Highway Fund changes. Higher fuel prices have decreased demand for gasoline and diesel fuel. The tax models have added fuel prices as an additional variable to help better capture the effect on fuel tax revenue. The forecast also recognizes the effect on the Highway Fund investment earnings of cash balances that have been drained by budget problems in the Department of Transportation's capital program.

The **Fund for a Healthy Maine (FHM)** revenue forecast was revised downward for the 2008-2009 biennium primarily based on an assumed continued delay in the receipt of tobacco settlement payments pending the outcome of litigation concerning the Master Settlement Agreement. The FHM revenue forecast also reflects a negative adjustment resulting from changes in the Global Insight's economic modeling for the forecast period. These negative adjustments are partially offset by assumed increases resulting from the FHM's share of the projected increase in gaming revenue from slot machines operated in association with the commercial race track in Bangor, and from assumed income from investments. The net result for the 2008-2009 biennium revenue forecast for the Fund for a Healthy Maine is a downward revision of \$26.5 million (\$13.5 million in FY08 and \$13.0 million in FY09). The projections for the 2010-2011 biennium are for growth of 8.0% and 5.5%, respectively, and assume for projection purposes that the State will prevail in the legal proceedings.

Note: The growth expected in the 2008-2009 biennium in tobacco settlement payments from the addition of the 10 annual "Strategic Contributions Payments" that begin in FY08 was already reflected in the base forecast.

In aggregate, the forecast for **Medicaid/MaineCare Dedicated Revenue Taxes** was revised upward for the forecast period. This revision was driven primarily by an upward adjustment in service provider tax dedicated revenue (i.e., that portion of the tax applied to private non-medical institutions (PNMI's), community support, day habilitation, personal support and residential training services) based on actual FY06 revenue and FY07 collections to date. The revised forecast also assumes a slight upward adjustment in hospital tax revenue. These positive adjustments in the MaineCare tax forecast are partially offset by downward revisions in nursing facility and residential treatment facility tax revenue based on actual experience.

Attachments

cc: Members, Revenue Forecasting Committee
Members, Consensus Economic Forecasting Commission
Jane Lincoln, Chief of Staff, Governor's Office
Rebecca Wyke, Commissioner, DAFS
Millie MacFarland, Clerk of the House
Joy O'Brien, Secretary of the Senate
David Boulter, Executive Director, Legislative Council
Legislative Staff Office Directors